Statement by

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Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to join this panel. The Committee should be commended for its continued leadership on the issue of financial services modernization. The question we will address today -- the regulatory framework for consolidation in the banking and brokerage industry -- is of great importance. I am pleased to have the opportunity to offer my views.

Although I am a lawyer practicing here in Washington, and I previously served as Director of the Division of Market Regulation at the Securities and Exchange Commission ("SEC"), I appear today in my personal capacity and not on behalf of my firm, any client or the SEC.

The goal of financial services modernization should be to achieve two related objectives. First, we should maintain and enhance investor confidence in our capital markets as those markets continue to expand through technological innovations and intense competition to introduce new and useful financial products. Second, we should ensure that our markets continue to serve their critical role of providing capital for companies, an important source of growth for our economy.

These twin objectives -- investor confidence and efficient capital availability -- require that any new regulatory structure should both ensure adequate investor safeguards are maintained and facilitate new capital raising techniques. To further these objectives, financial services reform should focus on creating a framework that will provide consistent and rational regulatory protection for investors as current market participants move beyond their traditional focus and functions. In addition, financial services reform should strive to provide banks and securities firms alike opportunities for market participation and competition on the basis of performance rather than differences in regulation, and should provide for the entrance of new market participants on an equal footing.

A regulatory structure built around the concept of functional regulation will further these objectives. Functional regulation allows the appropriate expert regulator to evaluate particular risks while at the same time providing the flexible provision of financial services regardless of the structure of market participants.

For example, as a general precept, securities activities can, and should, be conducted through a registered broker-dealer and regulated by the appropriate securities regulator. In turn, if the broker-dealer is part of a larger group of business entities, the securities regulator should cooperate with other regulators (e.g., insurance and banking authorities) to provide necessary information to evaluate group-wide risks. Through such cooperative regulatory efforts, investors in the same financial product can expect the same level of protection and have the same level of confidence in the market for that product, regardless of the corporate structure of the market participant on the other side of the transaction.

In this regard, the SEC already has considerable experience with the regulation of financial intermediaries that are part of a larger corporate group that offers a variety of different products. The SEC has found that its regulation is not impaired by such affiliations. Indeed, the SEC has developed a holding company risk-assessment program designed to facilitate gathering information relevant to its oversight of the regulated entity, while still allowing diverse organizational structures and avoiding an added layer of substantive regulation over the entire organization. Indeed, the combination of commerce and finance, from a securities perspective, has been an affirmative benefit to the capital markets rather than a liability.

A functional regulation approach also recognizes, and is responsive to, recent market developments. We can see all too plainly the considerable pressures toward consolidation within the financial services industry (e.g., technology, globalization, and asset management techniques). It appears that these pressures only will increase during the foreseeable future. We should be cautious, however, in assuming such consolidation is inevitable. For example, the push to develop so-called "financial supermarkets" during the 1980s never developed as predicted. The point, of course, is that markets by their nature are dynamic, and we should have a regulatory structure which facilitates, rather than impedes, that dynamism.

Functional regulation will enhance marketplace competition by allowing market participants to organize themselves as they best see fit to respond to marketplace developments, whether investor demands for services or company demands for capital. In this regard, it also will enhance the entrepreneurship and innovation which have been the hallmark of American capital markets. Moreover, by facilitating competition between various market participants, functional regulation will reinforce those key features of our capital markets.

In conclusion, the debate about financial services modernization often becomes a debate about which regulated entity can perform which service subject to what regulatory authority. Those are important questions which will affect significantly the policy objectives to be achieved. Nevertheless, meaningful reform should anticipate future growth and the unknowable future innovations. The overarching goal of such reform should be enhancing investor confidence in the capital markets so that companies can raise capital to promote growth in the economy. Judged by this standard, we should continue our traditional reliance on diverse, aggressive competition supplemented by minimum regulatory oversight to ensure investor confidence. Functional regulation achieves this goal and provides the added benefit of minimizing the possible spill-over effect of a perceived expansion of the financial safety net of deposit insurance.

I would be pleased to answer any questions the Committee might have.